Asia Credit

Earnings Review: CapitaLand Ltd ("CAPL")

Issuer Profile: Neutral (3)

Ticker: **CAPLSP**

Background

CapitaLand Ltd ("CAPL") is Singapore's leading real estate developer, operating across residential development, serviced residences, retail & office REITs and real estate fund management. Geographical segments are CL Singapore, Malaysia and Indonesia ("CLSMI"), CL China ("CLC"), CL Vietnam ("CLV") and CL International ("CLI"). CAPL reported SGD62.1bn in total assets as at 31 March 2018 and it is ~40%-owned by Temasek Holdings Ltd.

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Recommendation

- Prior trends of residential inventory declining persisted with likely impact on development revenue post 2018. Though stable q/q, leverage drifted higher since end-2016 on acquisitions, and potentially on further land banking. Sizable investment property portfolio provides comfort though minority interest surged post the consolidation of its REITs. We will retain our Neutral (3) Issuer Profile.
- When comparing the CAPLSP '24s with the recent CCTSP '25s and CAPITA '23s (we hold all three issuers at Neutral (3) Issuer Profile), we believe that the new CAPITA '23s is the most attractive, given the 1-year shorter duration and the benefit of being closer to the assets (CMT REIT debt versus CAPL HoldCo debt).

Relative Value:

Bond	Maturity/Call date	Net Gearing	Ask Yield	Spread
CAPLSP 3.8% '24	28/08/2024	49%	3.20%	72bps
CCTSP 3.327% '25	21/03/2025	61%	3.40%	88bps
CAPITA 3.2115% '23	09/11/2023	50%	3.15%	74bps

Indicative prices as at 7 May 2018 Source: Bloomberg
Net gearing based on latest available quarter

Key Considerations

- **Accounting changes and REIT consolidation**: Revenue was up sharply by 53.3% y/y to SGD1.38bn. It is worth noting that CAPL both restated its financial statements to adhere to SFRS (I) 15 accounting standards (this relates to how revenue for development assets are recognized, versus the previous Percentage of Completion method for domestic developments), as well as changed its segment disclosure to focus on geography instead of business segment. CAPL had also consolidated its two retail REITs (CMT, CRCT) as well as Raffles City Singapore ("RCS") from August 2017 onwards, which boosted total revenue on a y/y basis. As mentioned, effective 01/01/18 CAPL has reorganized its structure, and with primary focus (and reporting detail) on geographical segment. These are CL Singapore, Malaysia and Indonesia ("CLSMI"), CL China ("CLC"), CL Vietnam ("CLV") and CL International ("CLI"). Presentation by business segment (Residential & Commercial Strata, Retail, Commercial and Serviced Residences) is now secondary.

- **Singapore inventory depletion continues**: CLSMI saw revenue more than doubling to SGD602.1mn on the sale of further units at Victoria Park Villas (6 units, fully sold), Sky Habitat (16 units) and Marine Blue (4 units). CLSMI EBIT was 4.4% weaker y/y though at SGD338.9mn, absent the prior period gain on the bulk divestment of The Nassim. Looking forward, CLSMI's development revenue would likely decline due to falling levels of Singapore inventory. Already, residential units sold in Singapore fell to 40 units (1Q2017: 84 units) while sales value fell harder to SGD150mn (1Q2017: SGD504mn). 98% of CAPL's Singapore launched units have been sold (as of end-1Q2018). The main Singapore land bank would be Pearl Bank Apartments (which is in the process of being acquired) with a land cost of SGD929.4mn (SGD1,515 psf). Aside from this, CAPL also has a plot at Yio Chu Kang Road (GFA: ~210,000 sqft, ~80 units). Aside from CLSMI's development revenue though, it is likely that the segment also captures revenue contribution from CCT (SGD96.4mn), CMT (SGD175.2mn) as well as RCS (~SGD57.5mn). The contribution from these investment properties would total ~SGD329.1mn for the quarter and would be relatively stable.

- **Divestment gains mitigated weakening China development sales**: CLC reported revenue up 25.7% y/y to SGD563.4mn for the quarter. Residential units delivered during the quarter increased 9% y/y to 1,328 units, though value realized declined 35% y/y to RMB1.92bn on lower average selling prices. Revenue recognition pipeline looks healthy, with over 8,000 units sold totalling ~RMB15.1bn in value (of which ~70% will be recognized over the balance 9 months of 2018, or ~SGD2.2bn). Looking beyond 2018 though, with CAPL already selling 96% of its launched units in China, development revenue may fall. For 1Q2018, units sold fell 54% y/y to 998 units, while sales value fell 57% y/y to RMB1.68bn. CAPL indicated 5,725 units that are ready for launch over the balance of 2018 (though it should be noted that 3,069 of these units are attributed to the La Botanica at Xi'an, which CAPL only has an effective stake of 38%). China EBIT surged 45.5% y/y to SGD283.3mn, driven by divestment gains recognized on their sale of 20 non-core retail malls (+SGD35.4mn profit after tax & minority interest impact). The consolidation of CRCT also boosted both revenue and EBIT on a y/y basis.

- **JVs drove Vietnam, acquisitions drove International**: Though CLV reported a 9.8% y/y decline in revenue to SGD20.5mn, this was largely due to most of the unit deliveries done at JV developments (CAPL delivered 259 units versus 116 units in 1Q2017). Segment EBIT grew sharply to SGD46.4mn (1Q2017: 8.4mn) due to divestment gains. ~93 of CAPL's Vietnam launched projects have been sold. ~50% of SGD686mn in Vietnam pre-sales are expected to be recognized in the balance of 2018, though we note that several of these developments (such as Vista Verde, Kris Vue and Seasons Avenue) are held in JVs (and hence off balance sheet). For CLI, revenue was up 38.4% y/y to SGD198.1mn, due to various investment properties acquired in Germany and Japan. Segment EBIT fell 33.1% y/y to SGD44.4mn though, absent the divestment of two German assets the prior period.

- **Stable credit profile for now**: In aggregate, profit after tax was 6.3% higher y/y to SGD495.0mn. Operating cash flow (including interest service) was strong at SGD257.9mn on residential inventory monetization (1Q2017: SGD205.3mn operating cash outflow). Cash balance fell q/q by SGD535.0mn however, on share repurchases (SGD120.8mn), debt pay down (SGD171.1mn), dividends to REIT minority holders (SGD239.4mn) and investments (SGD240.1mn). Net gearing remained stable q/q at 49%. Short-term debt of SGD2.42bn is manageable given CAPL's SGD5.63bn in cash balance. That being said, we expect CAPL will be paying for its Pearl Bank Apartments acquisition in the near future. Assuming that the acquisition is fully debt funded, this would drive net gearing higher to pro-forma ~52%.

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Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

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To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

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